

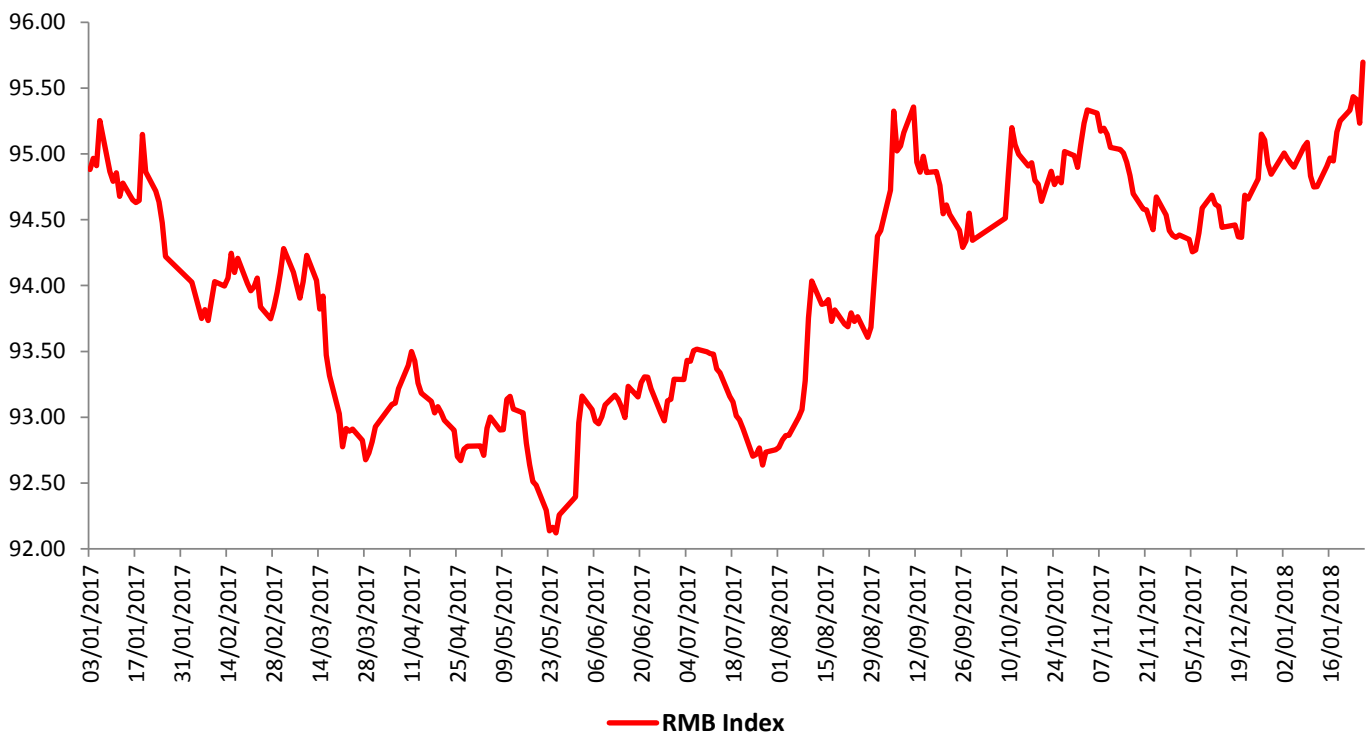
Highlight

In an increasingly fractured world, China's key economic policy advisor Liu He reinforced China's image as the leader of next phase of globalization. He said China will specially honour Paris agreement and will further integrate with world trade rule and ease market access. Domestically, Liu highlighted three critical battles faced by China in the next few years including preventing financial risk, targeted poverty reduction and environmental protection. Shadow banking and hidden debt for local government are two major problems China will deal with in the next few years. Meanwhile he also commits that China will keep leverage ratio under effective control in three year time.

In a violent move of broad dollar last week, the USDCNY tested 6.30. Nevertheless, the most notable movement was the spike of RMB index, which jumped to 95.70 last Friday, close to two and half year high. The jump of RMB index last week was also partially due to weak performance of Korean Won, which failed to appreciate meaningfully against the dollar year to date. As KRW accounts for more than 10% of basket weights in RMB index, the weaker KRW performance has partially contributed to recent spike of RMB index. Looking ahead, as RMB index approaches 96, market will closely monitor the reaction of the central bank to check whether there will be any intervention to slow down the appreciation.

In Hong Kong, housing completions decreased by 24.68% yoy in November 2017. Severe imbalance between pent-up demand and slowly increased private and public home supply led to continuous growth of housing prices despite cooling measures. Moving forward, we see two downside risks to the overheated housing market, including increasing supply and capital outflows which may push up borrowing costs and lead to stock market correction. On the other hand, exports and imports expanded by 6% yoy and 9% yoy respectively in December 2017. This indicates that trade activities would have supported 4Q GDP. With global economy to sustain its benign growth throughout 2018, we expect HK's trade sector will remain resilient and continue to support local economic growth. A weaker HKD against currencies other than greenback may also boost HK's exports. Nevertheless, China's economic slowdown, China's loosening of some import policies and the revival in Trump trade protectionism may translate into some downside risks to HK's trade sector. In Macau, visitor arrivals grew at its fastest pace since 2014 by 5.4% yoy in 2017. The sustained economic growth across Asia and improvement in infrastructure including the upcoming completion of HK-Zhuhai-Macau Bridge are expected to further support the tourism sector. Besides, a new wave of hotel and casino openings this year may encourage tourists to re-visit the gambling hub while also help to lure new visitors.

Chart of the week: The spike of RMB index to 95.70 last Friday may test China's comfort zone on pace of RMB appreciation.



Source: Bloomberg, OCBC

Key Events and Market Talk	
Facts	OCBC Opinions
<ul style="list-style-type: none"> China's key economic policy advisor Liu He said in 2018 Davos Economic Forum that China will fight three critical battles to achieve its target of building China as modern society. 	<ul style="list-style-type: none"> Liu He said China will continue its supply side reform, which has yielded some positive results as China's total factor productivity has stopped its decline and began to increase since 2016. In addition, Liu highlighted three critical battles faced by China in the next few years including preventing financial risk, targeted poverty reduction and environmental protection. Shadow banking and hidden debt for local government are two major problems China will deal with in the next few years. Meanwhile he also commits that China will keep leverage ratio under effective control in three year time. On the positive note, Liu said China has achieved marginally slower overall leverage ratio growth since 4Q 2017. And changing market expectation on implicit guarantee and moral hazard helped. Meanwhile, he also invited global community to participate in China's battle to control financial risk. On global economy, Liu reckoned synchronized global recovery but said the deep seed problems such as high debts, asset bubble and protectionism remain to be solved. He also said China will specially honour Paris agreement and will further integrate with world trade rule and ease market access.
<ul style="list-style-type: none"> The PBoC net withdrew CNY320 billion via open market operation last week as forward targeted reserve requirement ratio cut officially took effect. 	<ul style="list-style-type: none"> The forward targeted reserve requirement ratio cut, announced in late September 2017, took effect on 25 January, which was estimated to inject about CNY300 billion into the system according to Xinhua newswire. However, the overall liquidity situation was flush last week. As such, the PBoC withdrew the liquidity via regular open market operation. The net withdrawal of liquidity shows that there is no change of China's prudent monetary policy.
<ul style="list-style-type: none"> Hong Kong implements the Net Stable Funding Ratio (NSFR) requirement starting from 1 January 2018. It is required that a category 1 institution's NSFR should be no less than 100% and should be reported to HKMA on a quarterly basis. If a category 1 institution's NSFR falls below 100% but remains above 90% and the shortfall is rectified within one month, this will not constitute a contravention of the Banking (Liquidity) Rules. HKMA also makes certain modifications to the NSFR for the purpose of devising a stable or core funding ratio for application to category 2 institutions. Category 2 institutions should be required to maintain a modified NSFR of not less than 75% on average in each calendar month. 	<ul style="list-style-type: none"> As the coefficient for retail deposits is the highest among various types of funding, small to medium size banks may be prompted to lift deposit rates. Also, higher funding needs of small to medium size banks may also push up interbank lending rates. Therefore, the new rules are expected to have upward pressure on HIBOR.

Key Economic News	
Facts	OCBC Opinions
<ul style="list-style-type: none"> HK housing completions decreased by 24.68% yoy in November 2017 and increased by 22.3% yoy to 14751 units during the first eleven months of 2017. Severe imbalance between pent-up demand and slowly increased private and public home supply led to continuous growth of housing prices despite housing cooling measures. According to the latest study by Demographia, an urban planning policy 	<ul style="list-style-type: none"> Housing demand in HK has been elevated in three perspectives. Firstly, local investment demand has been boosted by wealth effect from stock market and housing market. Secondly, foreign investment sentiment has remained upbeat as Mainland investors with increasing wealth are eager to diversify their portfolio. Thirdly, a nearly two-decade low unemployment rate combined with benign real wage growth and developers' provision of mortgage loans has supported middle-class

<p>consultancy, housing affordability in HK ranked the lowest across the globe for the eighth consecutive year in 2017.</p>	<p>households to enter the market. Finally, annual growth of households has remained at or above 2.5% yoy since 1Q 2015 and resulted in huge pent-up demand. On the supply side, government's revenue relies heavily on proceeds from land sales. This damps government's incentive to loosen the rules restricting land use. Therefore, limited land supply results in continuous increase in land prices and in turn bolsters growth of home prices.</p> <ul style="list-style-type: none"> ▪ Moving forward, we see two downside risks to the overheated housing market, including capital outflows and increasing supply. On the one hand, capital rotation from emerging market to developed market is likely should global central banks start to tighten their monetary policy. If this is the case, a resultant correction in stock market and increase in local interest rates are likely to deter some investment demand. On the other hand, housing starts increased by 11.57% yoy to 21433 units over the first eleven months of 2017 and are set to surpass 20000 units for the second consecutive year. This indicates higher private home supply in the coming years. Besides, regularized purchase of subsidized flats by White Form applicants and increasing supply of subsidized homes for residents living in public rental flats may help to shift some owner-occupier demand from private housing market. Still, housing correction will likely be limited in the longer term given investment demand from Mainland China and increasing local population.
<ul style="list-style-type: none"> ▪ HK's exports and imports expanded by 6% yoy and 9% yoy respectively in December 2017 and grew by 8% yoy and 8.7% yoy respectively in 2017 as a whole. As a result, trade deficit widened to its largest level since 2014 at HK\$481.1 billion in 2017. 	<ul style="list-style-type: none"> ▪ On the one hand, imports increased on a broad basis in December due to the effect of Christmas Holiday and higher commodity prices. Specifically, imports from Taiwan and Malaysia, two of the major trading partners, increased by 30.3% yoy and 60.7% yoy respectively in December. On the other hand, the growth of exports to Mainland China decelerated notably from 10.1% in November to 1.7% in December. This is in line with the weaker-than-expected import data of China for the same month. Despite that, overseas shipments to Japan (+10.8% yoy), India (+66.6% yoy) and Vietnam (+10% yoy) all sustained their robust growth. Furthermore, exports to the USA increased at the fastest pace since February 2015 by 11.5% yoy while those to Germany registered double-digit annual growth for the fourth consecutive month by 28.7% yoy. More notably, exports and imports of "electrical machinery, apparatus and appliances, and electrical parts thereof" advanced by 6.8% yoy and 15.4% yoy respectively in December. ▪ Taken all together, we believe that recent slowdown in China's trading activities will be transitory. With global economy to sustain its benign growth throughout 2018, we expect HK's trade sector will remain resilient and continue to support local economic growth. A weaker HKD against currencies other than greenback may also boost HK's exports. Nevertheless, China's economic slowdown and its loosening of some import policies may have some downward pressure on HK's exports. Also, the revival in Trump trade protectionism could put a lid on HK's trade activities.
<ul style="list-style-type: none"> ▪ Hong Kong total net exports of gold to China dropped for the fifth consecutive month by 35.2% yoy to 30.47 metric tons in December 2017. 	<ul style="list-style-type: none"> ▪ Date back to 2015, China imported a net 774 metric tons from Hong Kong, representing a 3.1% yoy increase. This was attributed to capital exodus associated with RMB exchange rate

	reform. After that, further RMB exchange rate reform and tightened supervision over cross-border capital flows helped to improve RMB outlook. In 2017 as a whole, Hong Kong exported a net 602 metric tons to China, the lowest level since 2012. This reinforces that capital outflow risks have been well-contained.
<ul style="list-style-type: none"> Macau: The number of total visitor arrivals increased by 8.5% yoy in December 2017 and grew at its fastest pace since 2014 by 5.4% yoy in 2017 as a whole. Overnight visitors and same-day visitors increased by 9.9% yoy and 0.7% yoy respectively over 2017. 	<ul style="list-style-type: none"> Rebound of the tourism activities is mainly attributed to Asia's broad-based growth. First, visitors from Mainland China increased 8.5% yoy in 2017 on the bank of China's resilient growth. The share of Mainland visitors in total visitors averaged at its record high of 68%. Second, the number of visitors from South Korea climbed for the 19 consecutive months in December 2017 and edged up by 32% yoy in 2017. Third, Japanese visitors increased by 9.4% yoy in 2017. On the contrary, visitors from Hong Kong and Taiwan decreased by 4% yoy and 1.3% yoy respectively last year. For Taiwanese tourists, the decline may be due to a high base effect. Differently, high accommodation and transportation costs are believed to be the main reasons behind the reduction in HK tourists. Looking ahead, the sustained economic growth across Asia and improvement in infrastructure including the upcoming completion of HK-Zhuhai-Macau Bridge are expected to further support the tourism sector. Besides, a new wave of hotel and casino openings this year may encourage tourists to re-visit the gambling hub while also help to lure new visitors.

RMB	
Facts	OCBC Opinions
<ul style="list-style-type: none"> In a violent move of broad dollar last week, the USDCNY tested 6.30. Nevertheless, the most notable movement was the spike of RMB index, which jumped to 95.70 last Friday, close to two and half year high. 	<ul style="list-style-type: none"> As we highlighted in the previous report, the pressure has been transferred from the USDCNY to RMB index without the use of counter cyclical factor. The jump of RMB index last week was also partially due to weak performance of Korean Won, which failed to appreciate meaningfully against the dollar year to date. As KRW accounts for more than 10% of basket weights in RMB index, the weaker KRW performance has partially contributed to recent spike of RMB index. Looking ahead, as RMB index approaches 96, market will closely monitor the reaction of the central bank to check whether there will be any intervention to slow down the appreciation.

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